

Title Insurance: A Risk Management Tool

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Introduction

Title insurance is a specialised type of insurance providing protection against risks inherent in the real estate transaction that may affect a home owner's ownership or use of the property they are purchasing or currently own.

Title insurance may be described as a contract of *indemnity* whereby the title insurer indemnifies the insured (being the owner of a legal right in real property) against actual loss incurred by the insured as a result of any unknown title defect or other risk covered in the policy as at the date of settlement.

Clients look to their settlement agent to provide advice in respect of the risks to which they are exposed. Typically, this advice is limited to matters disclosed in the contract of sale or that are discoverable by searches and enquiries.

Further, whilst the Torrens Title system is designed to protect a buyer against any defect in the registration system, it will not protect a buyer against many of the practical risks inherent in property transactions which fall well outside of the safety of the Torrens System.

Title insurance is designed to equip settlement agents with a "risk management tool" to reduce or eliminate these risks in the real estate transaction.

About Stewart Title Limited

Stewart Title Limited is wholly owned by Stewart Title Guaranty Company the primary underwriter for Stewart Information Services Company. The Stewart group of companies traces its origins back to 1893 in Texas, USA. The group now has more than 8000 issuing offices worldwide across 16 countries.

Stewart Title Limited is regulated by the Australian Prudential Regulation Authority (APRA) and is licensed to operate as a title insurer in all states and territories in Australia. Stewart Title Limited offers title insurance policies for both lenders and buyers of residential and commercial property. Insurance for buyers of commercial properties will be introduced by Stewart Title in the near future.

What Risks are Covered?

The insured is protected against **actual loss** incurred by the insured as a result of unknown risks or defects which existed prior to or at the date of settlement. Some of these covered risks include loss caused by:

- illegal/unapproved building work;
- encroachments;
- zoning non compliance;
- unsatisfied conditions of a development consent;
- non compliance with the terms of a positive and/or restrictive covenant or easement;
- unregistered rights of way and easements or non compliance with registered rights of way and easements;
- fraud and forgery;
- unpaid rates and taxes resulting in a charge on the land².

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² This is only a summary of the coverage offered by a Stewart Title Residential Purchaser Policy. For complete coverage, terms and conditions you should refer to the Policy or contact Stewart Title's Underwriting Department on (02) 9081 6200.

Cover is also provided to the insured for the following risks where they arise or come into existence after the date of settlement:

- fraud and forgery;
- encroachments from neighbouring property;
- post settlement dealing registrations by third parties.

In addition to indemnifying the insured from actual loss, Stewart Title will also defend the insured's title covering the **legal costs and expenses** incurred in that defence³. These costs would be in addition to any liability the insurer may have in respect of the indemnity amount contained in the policy.

The policy amount is based on the purchase price of the property and will automatically increase in line with the market value of the land up to a maximum of 200% of the policy amount. The insured pays a **one time premium** based on the purchase price of the property and is protected forever from the date of settlement. Premiums for properties in Victoria begin at \$363 (inclusive of 10% GST and 10% stamp duty) for properties valued up to \$500,000.

The insured can make a claim with ease under our **no fault claims** process. The advantage of claiming under a Stewart Title policy rather than claiming against a settlement agent's professional indemnity insurance or commencing proceedings against a local authority is that they are not required to prove fault or negligence in order to make a claim. As long as the insured has suffered "actual loss" as a result of a matter covered under the Stewart Title policy and the insured is able to provide proof of loss then Stewart Title is obligated to pay the claim.

Stewart Title may then pursue the party at fault under its rights of subrogation, although Stewart Title will **waive its rights of subrogation** against settlement agents⁴.

In addition to the waiver of subrogation, Stewart Title provides a standard wholesale **indemnity** for settlement agents in the event that the buyer is insured under a title insurance policy but nonetheless elects to pursue the settlement agent thereby triggering a claim under his or her professional indemnity insurance policy⁵.

Importantly there is **no excess** payable by the insured when they make a claim.

Example of Cover – Illegal Building Work

You act for a purchaser. The vendor's statement does not disclose that any building permits have been issued in the past seven years.

You proceed to settlement.

Following settlement, the purchaser carries out further development on the land which prompts Council to inspect the property. Following that inspection, Council informs the purchaser that the existing structure, which was built by the previous owner, was never approved by Council and must be upgraded or demolished.

Council issues an order requiring the buyer to demolish or upgrade the existing structure.

What is the "Actual Loss"?

In relation to the above example, Stewart Title would be obligated to indemnify the insured for any "actual loss" arising from the upgrading and demolition order. Such loss might include:

- The costs of upgrading or correcting or **replacing** the illegal structure so that they comply with relevant building standards and Council approval;

³ See clause 1.2 of the Stewart Title Policy.

⁴ Except in circumstances where the settlement agent has been grossly negligent or criminal.

⁵ For specific details of the nature and extent of the indemnity enquiries should be made of Stewart Title Limited.

- If the illegal structure may not be upgraded, corrected, or replaced then the loss in the market value of the property for the deprivation of the use of the illegal structure;
- In circumstances where the insured has entered into a contract to sell the property and prior to completion the buyer elects to rescind the contract because of the issue of an upgrading or demolition order, then the actual loss would include (for example) the interest payments on any bridging loan secured by the insured to purchase a new home, any subsequent shortfall in the contract price if a subsequent buyer is found (the marketability coverage).

The Benefits of Title Insurance

The benefit for buyers is that following settlement, Stewart Title, rather than the buyer, will assume the risk of the existence of any unknown illegal building works, and will accordingly indemnify the buyer against actual loss caused by a subsequent demolition or upgrading order following settlement.

Custom Underwriting & Affirmative Coverage for Known Defects

Whilst Stewart Title typically excludes from coverage any risk which is known to the insured but which is *not* disclosed⁶, Stewart Title may provide “affirmative coverage” (for no additional premium) on a case by case basis for risks and defects which are discovered prior to settlement and are disclosed to Stewart Title.

Stewart Title’s ‘custom underwriting’ of known risks represents a distinct benefit to buyers in circumstances where a defect is identified during the course of a conveyancing transaction.

Where a known risk is identified, enquiries should be made of Stewart Title to determine whether “affirmative coverage” may be offered and the extent of that cover.

Not Just Title Insurance – A Comprehensive Risk Management Solution

The Stewart Title solution is a comprehensive risk management solution. In addition to our title insurance product, we have developed various support tools, including the development of a Risk Management Toolkit that assists in seamlessly integrating title insurance as an option in the conveyancing transaction.

Conclusion

Many of the practical risks assumed by buyers today fall well outside of the safety of the Torrens System. Ideally, the basis of any system of title by registration is certainty of title, so that all relevant interests are noted on a certificate which reflects the exact state of the title at any moment in time. In practice, however, this is not the case since many of the risks faced by buyers today are not discoverable by a simple search of the title, as is the object of the Torrens System.

Illegal building works, boundary discrepancies, zoning and planning non compliance, and other “off title” risks continue to present practical problems for buyers and their settlement agents. In many ways, ‘title’ insurance is more accurately described as “conveyancing risk” insurance and in this regard, should be regarded by settlement agents as a risk management product available for intending buyers to ‘plug’ some of the gaps in the Torrens title system.

⁶ See for example Clause 3.1 (e) of the Stewart Title policy.